No. 17,387

IN THE

United States Court of Appeals

For the Ninth Circuit

UNITED STATES OF AMERICA,
Appellant,

vs.

CHARLES E. and LOIS W. ROSEBROOK,
Appellees.

On Appeal from the Judgment of the United States District Court for the Northern District of California

REPLY BRIEF FOR THE APPELLANT

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I

THE ISSUE PRESENTED BY THIS APPEAL IS WHETHER THE DISTRICT COURT ERRED IN APPLYING THE LAW RELATING TO JOINT VENTURES AND NOT, AS TAXPAYER CONTENDS, WHETHER THE EVIDENCE SUPPORTS THE FINDINGS

The taxpayer attempts to avoid the issue presented by this appeal by contending (Br. 8-11) that the question involved is merely whether there is adequate evidence to support the District Court's finding that she was not personally engaged in the business of selling real estate. In so arguing and in asking this Court to

decide the case on that issue, the taxpayer ignores (and asks the Court to ignore) both the facts relating to the joint venture and the Government's contention that the court below erred in applying the law of joint ventures. Contrary to taxpayer's assertion, this case cannot be described as one merely involving a (Br. 11) "simple question of fact in which the District Court's decision is adequately supported by the record" for the Government does not challenge the findings; rather the case must be decided on the question of whether the District Court correctly determined the legal and tax consequences of the taxpayer's participation in the joint venture.

II

TAXPAYER'S SUGGESTION THAT THE DISTRICT COURT DID NOT MEAN WHAT IT SAID IN USING THE TERM "JOINT VENTURE" IS WITHOUT MERIT

The taxpayer suggests (Br. 11-19) that the District Court, in holding that the San Bruno land was acquired and sold pursuant to a joint venture, did not use that term in its accepted sense of an undertaking for profit but rather meant "joint ownership". We submit that the taxpayer has placed an alien meaning on the term which the courts have carefully avoided and which, as a reading of the opinion below demonstrates, was not used by the District Court.

The land here was nominally held by the venturers as tenants in common. If the court below had intended to hold that there was only joint ownership, we sub-

mit that it would simply have held that the parties were co-tenants, and would have avoided a term of art such as joint venture. Moveover, on taxpayer's motion (R. 110) to strike defendant's Exhibit B the court ruled (R. 120) that it would strike the exhibit only if it found that there was no joint venture or agency relationship between taxpayer and her father. Since the court not only did not strike exhibit but relied on it in its opinion and findings of fact, the court obviously found that there was a joint venture in the sense of joint enterprise empowering one venturer to act on behalf of and for another.

The principal distinction between joint ownership and joint venture is that in the former there is no intent to engage in a joint enterprise. *Gilford v. Commissioner,* 201 F. 2d 735 (C.A. 2d); *Henning v. Cox,* 148 F. 2d 586 (C.A. 5th); *Estate of Appleby v. Commissioner,* 41 B.T.A. 18, affirmed on other grounds, 123 F.2d 700 (C.A. 2d); 30 Am. Jur. Joint Adventures, Sec. 5.

The April 23, 1953, memorandum (Appendix C)[1], relied upon by the court below as a correct expression of the parties' intentions, shows that they intended to engage jointly and in concert in buying and selling the San Bruno tract. The memorandum states how the parties planned to acquire the San Bruno tract; that they planned to sell none of it until the six

[1]This reference is to Appendix C of the Government's main brief. Through a typographical error, the phrase "trusts for their children" was not lined out in Appendix C, although the copy of the memorandum introduced in evidence did contain this lined alteration.

months capital gain holding period had elapsed; that they planned to sell it to a corporation to be controlled by the principal parties involved and to sell some of it to outside parties; that the corporation would subdivide some of the land and would also use some for construction of business areas. The memorandum further stated that the parties agreeing thereto represented other interests which they controlled and for whom they were acting;[2] that all parties were flexible and would go along with whatever future course of conduct was desirable or could be worked out; and that all transactions would be carried out in the most advantageous tax manner.

The common enterprise outlined in the memorandum had all the elements of a joint venture: there was a community of interest in the enterprise, a sharing of profits and losses[3], joint participation in the affairs of the venture[4], and a close relationship between the

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[2]Plaintiff's Ex. 2 lists the following persons as participants as of June 30, 1955 (other than those named in the memorandum): Gerhard J. Bundlie, trustee of four trusts; Frank F. Burrows, trustee of one trust; Katherine Anne Williams; Lois Williams Rosebrook; George Wesley Williams III; Conway & Culligan Development Co.; American Homes Development Co.; G. W. Williams Co.

[3]The right to share profits implies a sharing of losses. *Nels E. Nelson, Inc. v. Tarman,* 163 C.A. 2d 714, 726, 329 P.2d 953, 958-959. However, the probability of losses under this joint venture, which was committed to selling the land at a fixed price to a particular buyer (Consolidated), was rather remote.

[4]The venturers do not have to have equal control over the conduct of the enterprise. *Foster v. Keating,* 120 C.A. 2d 435, 452, 261 P.2d 529, 539. And the venturers, as in this case, may grant authority to one or more of their number to act for them. *Stilwell v. Trutanich,* 178 C.A. 2d 614; 3 Cal. Rptr. 285. See defendant's Exhibit E, which is a power of attorney to three of the venturers to act for the venture.

parties. *Lasry v. Lederman,* 147 C.A. 2d 480, 485-488, 305 P.2d 663, 666-667; *James v. Herbert,* 149 C.A. 2d 741, 748, 309 P.2d 91, 95. The necessary intent of the parties to form a joint venture (*Lasry v. Lederman, supra; Haley v. Commissioner,* 203 F.2d 815 (C.A. 5th)) is found in both the April 23rd memorandum as well as in the parties' conduct in jointly selling 884 acres to Consolidated on February 10, 1954, and 80 acres in August, 1956, and in jointly leasing the property, banking the rents, and paying expenses. (R. 23-24.) The District Court's finding that there was a joint venture or enterprise (and not merely joint ownership) is amply supported by the facts.[5]

There is no question that taxpayer's trust was a member of the venture. The trust was one of the controlled interests referred to in the April 23rd memorandum and was represented by taxpayer's father, the trustee. Taxpayer's father, George Williams, as trustee, invested $7,000 of trust funds in the venture; as trustee, he also executed, along with the other venturers, a power of attorney (Deft. Ex. E) to three of their number (one of which was himself) for management of the venture. (R. 21-22.) On the trust's dissolution, therefore, taxpayer as beneficiary received the property that the trust held, which included *inter alia*

[5]This finding is in the court's opinion. (R. 14, 17.) As pointed out in our main brief, the court erroneously reasoned that because the parties formed a joint venture and not a partnership, the taxpayer must prevail (although it indicated that the Government would have prevailed had there been a partnership (R. 17)). The court apparently did not think it necessary therefore to include in its findings of fact and conclusions of law more than its holding (R. 25) that there was no partnership.

an interest in the joint venture. Manifestly, she did not receive something that the trust itself did not possess, i.e., she did not receive the ownership of an interest in the land independent of the joint venture.[6]

Even if the taxpayer's father did not inform her when he dissolved the trust that she was receiving an interest in a joint venture which was obligated to sell substantially all of its land to Consolidated, and that a sale was impending, taxpayer was bound by her trustee's acquisition of an interest in the venture and hence by the venture's purposes and commitments. *Werner v. United States,* 188 F.2d 266 (C.A. 9th). In any event, taxpayer ratified and accepted the acts of her father as trustee. (Joint Ex. 5-E.) Moreover, as a practical matter, there was no doubt that taxpayer (who had little knowledge of real estate) would follow her real estate-dealer father's suggestion with respect to sales by the venture to Consolidated. (R. 50, 53, 56-58, 94-95.)

It should also be noted that after the trust was dissolved and taxpayer received her interest in the venture in her own name, she fully participated in, and was accepted by, the venture.[7] She consented to the collection of rents by Mr. Crane (the venture's manager) and the deposit of these amounts in a com-

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[6]The fact that the land was held by the venturers (including successively the trust and then the taxpayer) as tenants in common is of no significance because the principles of joint venture apply irrespective of how title to the property is taken. *Larson v. Thoreson,* 36 C.2d 666, 226 P.2d 571.

[7]Taxpayer even referred to her fellow participants in the venture as "members". (R. 56.)

mon bank account from which various items of expense were paid; she and the other venturers forwarded their proportionate share of taxes and interest to Mr. Crane for payment, received semi-annual statements of the venture's financial status, and other intermittent reports; taxpayer even participated in the conduct of the enterprise by notifying Crane that a proposed sale of top soil was being made at too low a price. Most importantly, taxpayer joined with the other venturers in the August, 1956, sale of 80 acres to Consolidated for construction of a shopping center. (R. 23-24, 39, 41, 55-56, 58-59; Pltf. Ex. 2.)

Taxpayer seeks to find support in the recent Tax Court's decision in *Berryman v. Commissioner,* 37 T. C. No. 6, for her argument that the court did not mean joint venture when it used that term. *Berryman* involved taxpayer's sister who also received a one percent interest in the San Bruno joint venture upon dissolution of a trust for her benefit. The Tax Court held that Mrs. Berryman's income from the sale to Consolidated was capital gain and not ordinary income, relying heavily on the District Court's opinion and findings in the case at bar.

The Commissioner filed a petition for review by this court of *Berryman* on December 21, 1961. Although we have not yet seen the record in *Berryman,* if the facts are substantially the same as those at bar (as the Tax Court's opinion states) it follows that taxpayer's sister and her trust were necessarily successive members of the joint venture and that she too must report her distributive share of the venture's

income from the sale of the 884 acres as ordinary income.

Taxpayer also relies on the District Court's conclusion that she was not holding the property for sale to customers because neither she nor her trust had any interest in Consolidated. This conclusion, we submit, is of little importance in light of the court's finding that taxpayer was a member of a joint venture and of its holding with respect to the purpose of the principal and active venturers. (R. 14-15, 17.)

The purpose of the active members of the venture, as the court found (R. 14-15, 17), was to subdivide and sell part of the San Bruno tract through use of Consolidated. The active venturers were all otherwise engaged in the real estate subdivision business. (R. 14.) The court properly recognized that in acting together to buy the land for subdivision by them through Consolidated the active members were engaging in the conduct of that business, albeit jointly. The trial court quite accurately described the venture's function as a "step in carrying on their business" (R. 17) and correctly looked to the substance of the entire transaction which is controlling for tax purposes. Significantly, the taxpayer here does not challenge the court's conclusion in this respect.

The court below, however, erroneously held that (R. 17) while the purpose of the active members would be imputed to the inactive participants in their business if there had been a partnership, a different rule applies in the case of a joint venture. In this regard, the court erred, for as we have pointed out in

our main brief (pp. 13-22), there is no difference between a joint venture and a partnership under the tax law.[8]

Taxpayer argues (Br. 19-22), in effect, that the District Court's finding that there was a joint venture does not advance the Government's cause because the intention or purpose of the individual partners is controlling with respect to partnership property. Taxpayer suggests that the character of an item of partnership property is determined in the individual partner's hands rather than in the partnership's hands. Taxpayer quotes and relies on Section 702(b) of the 1954 Code. Although that section is technically not applicable to the sale under consideration,[9] it is declaratory of prior law, and thus its provisions are relevant to this discussion.

Section 702(b) provides that the character of partnership items of income, gain, loss

> shall be determined as if such items were realized directly from the source from which realized by

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[8]It should be noted that the purpose of the active venturers with respect to that part of the San Bruno tract purchased for investment purposes is also properly attributable (through the venture) to the inactive venturers. Thus, the 80 acres sold to Consolidated for construction of a shopping center by the principal venturers was not held for sale to customers, and the inactive venturers realized capital gain in participating in the venture and in joining the active members in this investment activity. Taxpayer's reporting of that income as capital gain has not been challenged. (R. 46-47.)

[9]Section 702 is part of Subchapter K of the 1954 Code. That subchapter is generally applicable to partnership taxable years beginning after December 31, 1954, and to any part of a partner's taxable year falling within such partnership taxable year. See Section 771(a) of the 1954 Code. Since the sale here under consideration occurred on February 10, 1954, it clearly is not subject to the 1954 Code provisions.

the partnership, or incurred in the same manner as incurred by the partnership.

We submit that that section, and Section 702(a) which requires the segregation of partnership gain on sale of its capital assets from its ordinary income, and the accompanying Committee Report (also relied on by taxpayer), all clearly reveal that partnership income is originally characterized at the partnership level and then reported by the partner as if he had earned it, and that each partner does not, as taxpayer contends, separately characterize his income from the partnership. The paragraphs from the Committee Report accompanying Section 702 (S. Rep. No. 1622, 83rd Cong., 2d Sess., pp. 89-90 (3 U.S.C. Cong. & Adm. News (1954) 4621, 4722)) which are set forth in the margin show this to be the case.[10]

It is interesting to note that taxpayer's position is supported by no case law. *Commissioner v. Paley,* 232 F. 2d 915 (C.A. 9th), certiorari denied, 352 U.S.

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[10]"The items required to be segregated retain their *original* character in the hands of the partner as though they were realized directly by him from the same source from which realized by the partnership and in the same manner. After excluding the items required to be separately treated, the remaining income or loss, which corresponds to the ordinary income or loss of the partnership under present law, is attributed to the partners.

"The computation of partnership income is generally on the same basis as existing law. The partnership is allowed the usual business deductions, but is denied the deductions peculiar to individuals.

"Both versions of the bill provide that all elections with respect to income derived from a partnership * * * [with one exception] are to be made at the partnership level and not by the individual partners. This rule recognizes the partnership as an entity for purposes of income reporting. *It avoids the confusion which would occur if each partner were to determine partnership income separately for his own purposes.*" (Italics added.)

838, the only case cited by taxpayer with respect to this argument, holds that a partner's distributive share of partnership gains from property used in its trade or business must be offset against the partner's individual losses from property used in his own trade or business. *Paley* not only refutes taxpayer's contention but it supports our position by indicating that the nature of partnership income is determined by the partnership's own trade or business and that the income is characterized in its hands.

We believe that our position in this case not only correctly reflects the law, but that it is equitable in that it treats all taxpayers who are jointly engaged in the same business in the same tax manner.

III

THE MEMORANDUM OF APRIL 23, 1953 WAS PROPERLY ADMITTED IN EVIDENCE BECAUSE IT WAS PROOF OF THE TERMS OF AN AGREEMENT BEARING ON THE ISSUES INVOLVED

The taxpayer complains (Br. 22-23) that the District Court improperly admitted the April 23rd memorandum. The memorandum states and describes an oral agreement reached at a meeting that day (April 23, 1953) of George Williams, Martin Wunderlich, Andrew Conway, and Thomas Culligan, with Robert Crane present. In addition to themselves, these persons were representing various interests including the taxpayer's trust. (Appendix C.) The agreement described in the memorandum, which the Government

successfully contended was a joint venture agreement, supplemented another agreement (which was in writing) of that date (Deft. Ex. A) providing for the purchase of the stock of San Bruno Lands, Inc. by the aforementioned venturers. The memorandum carries initials of the parties thereto on both of its pages. Prior to introduction of the memorandum, Joint Exhibit 2-B was admitted in evidence. That exhibit is the Declaration of Trust by which George and Hortense Williams, taxpayer's parents, created the trust for the benefit of taxpayer. It granted the named trustee, George Williams, broad powers to deal with and invest the corpus.

One of the issues below was whether a joint venture existed with respect to the purchase and sale of the San Bruno land in which taxpayer's father, as trustee, was a member. The memorandum as evidence of that joint venture agreement,[11] clearly was admissible and was not hearsay under the well established rule that the terms of an agreement which is in issue under the substantive law may be proved, as Wigmore states (VI Wigmore on Evidence (3 ed.), Sec. 1770), "without violation of the Hearsay rule because they are not offered to evidence the truth of the matter that may be asserted therein."

In *Paddock v. United States,* 79 F. 2d 872, 874, this Court held that statements between the taxpayer and his daughter were admissible because they fixed the

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[11]It should be noted that George Williams identified his initials on both pages of the memorandum thus authenticating it (R. 82), and that a copy was offered pursuant to a stipulation among counsel that copies could be admitted in evidence (R. 79).

terms of an employment contract, the existence of which was germane to the question of taxpayer's income tax liability. Similarly, the memorandum initialled by the principal parties in their individual and representative capacities was admissible as evidence of the joint venture agreement relevant in determining whether taxpayer and her trust had realized ordinary income on the sale of the San Bruno land because of participation in the joint venture.

The memorandum of April 23rd at bar is distinguishable from the statements in the cases apparently relied on by taxpayer and cited in Appendix C to her brief. Those cases did not involve an agreement which was a part of the details of the issue under the substantive law, nor was an author and party to the writing in court and available for examination with respect to the agreement and the writing. The latter reason also is sufficient to prevent the memorandum from being considered as hearsay. McCormick on Evidence (1954 ed.), pp. 457, 464. The cases of *Niederkrome v. Commissioner,* 266 F. 2d 238 (C.A. 9th), certiorari denied, 359 U.S. 945 and *Standard Oil Co. of California v. Moore,* 251 F. 2d 188 (C.A. 9th), certiorari denied, 356 U.S. 975, relied on by the taxpayer are further clearly distinguishable because of the absence in court of the author or party to the writing, necessitating the attempted reliance in those cases on the business records exception to the hearsay rule.

CONCLUSION

For the reasons stated above, the judgment of the District Court is erroneous, shou d be reversed, and judgment should be entered for the United States.

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